

## PAPER – 6 : AUDITING AND ASSURANCE

*Question No.1 is compulsory.*

*Attempt any **four** questions from the remaining **five** questions.*

### Question 1

*State with reasons whether the following statements are correct or incorrect:(Answer any Seven)*

- (a) In an automated environment, the relationship between the application controls and the General IT controls over IT systems are not interrelated.*
- (b) Historical financial information relates to financial information based on assumptions about occurrence of future events and possible actions by an entity.*
- (c) The auditor shall assemble the audit documentation in the audit file and complete the administrative process of assembling the final audit file before the date of the auditor's report.*
- (d) Where a firm is appointed as the auditor of a company, the report is signed only in the personal name of the partner signing the report.*
- (e) The term "Analytical Procedures" means evaluation of financial information through analysis of plausible relationships among financial data and non-financial data.*
- (f) A company should disclose in its Annual Report, the shares in the company held by each shareholder holding more than 10 percent shares specifying the number of shares held.*
- (g) As per SA 240, the primary responsibility of an auditor is to detect fraud and error in the financial statements.*
- (h) Mr. T, the director of A Ltd., has purchased an old car belonging to the company against the cooling equipment belonging to the director, which is given to the company as consideration for the car. The auditor is not required to include this in his CARO report.*

**(7 x 2 = 14 Marks)**

### Answer

- (a) Incorrect:** The relationship between the application controls and the General IT Controls is such that General IT Controls are needed to support the functioning of application controls, and both are needed to ensure complete and accurate information processing through IT systems. These two categories of control over IT systems are interrelated.
- (b) Incorrect:** Historical financial information relates to information expressed in financial terms of an entity about economic events, conditions or circumstances occurring in past periods. Whereas financial information based on assumptions about occurrence of future events and possible actions by an entity relates to prospective financial information.

- (c) **Incorrect:** The auditor shall assemble the audit documentation in an audit file and complete the administrative process of assembling the final audit file on a timely basis after the date of the auditor's report. The completion of the assembly of the final audit file after the date of the auditor's report is an administrative process that does not involve the performance of new audit procedures or the drawing of new conclusions.

**Alternative reason:** An appropriate time limit within which to complete the assembly of the final audit file is ordinarily not more than 60 days after the date of the auditor's report.

- (d) **Incorrect:** Where the firm is appointed as the auditor, the report is signed in the personal name of the auditor and in the name of the audit firm. The partner/proprietor signing the audit report also needs to mention the membership number assigned by the Institute of Chartered Accountants of India. They also include the registration number of the firm, wherever applicable, as allotted by ICAI, in the audit reports signed by them.

**Alternative Solution:**

As per section 145 of the Companies Act, 2013, the person appointed as an auditor of the company shall sign the auditor's report or sign or certify any other document of the company. Whereas if a firm is appointed as an auditor of a company, only the partners who are chartered accountants shall be authorised to act and sign on behalf of the firm.

The partner signing the audit report also needs to mention the membership number assigned by the Institute of Chartered Accountants of India. They also include the registration number of the firm, wherever applicable, as allotted by ICAI, in the audit reports signed by them.

- (e) **Correct:** As per Standard on Auditing (SA) 520 "Analytical Procedures", the term "analytical procedures" means evaluations of financial information through analysis of plausible relationships among both financial and non-financial data. Analytical procedures also encompass such investigation as is necessary of identified fluctuations or relationships that are inconsistent with other relevant information or that differ from expected values by a significant amount.
- (f) **Incorrect:** Schedule III to the Companies Act, 2013 requires the company to disclose- "shares in the company held by each shareholder holding more than **5 per cent** shares specifying the number of shares held" in notes to accounts.
- (g) **Incorrect:** As per SA 240 "The Auditor's Responsibilities Relating to Fraud in an Audit of Financial Statements", the primary responsibility for the prevention and detection of fraud rests with both those charged with governance of the entity and management. An auditor conducting an audit in accordance with SAs is responsible for obtaining reasonable assurance that the financial statements taken as a whole are free from material misstatement, whether caused by fraud or error.
- (h) **Incorrect:** The auditor is required to report the same as per clause (xv) of Paragraph 3 of CARO, 2020, "whether the company has entered into any non-cash transactions with

directors or persons connected with him and if so, whether the provisions of section 192 of Companies Act have been complied with”.

**Question 2**

- (a) S& Co., Chartered Accountants, are appointed as the auditors of ABC Ltd. CA S, the engagement partner, has come across the following while verifying equity share capital of the company:

- (i) He noticed that some of the equity shares are held by promoters.
- (ii) Some shares are issued as sweat equity shares to the employees.

*What is the meaning of sweat equity shares?*

*What are the disclosure requirements of such promoter's shareholding?* **(4 Marks)**

- (b) CA P is appointed as an auditor of XYZ Limited for the F.Y. 2021-22. The management of XYZ Limited has requested the auditor to change the terms of original engagement as the company has diversified its business and few new products have been introduced by the company. Can CA P agree to the request made by the management? Under which circumstances can the client make a request to the auditor for a change in the terms of engagement? **(4 Marks)**

- (c) What are the matters that the auditor shall consider while designing an audit sample? **(3 Marks)**

- (d) In an automated environment, General IT controls are policies and procedures that relate to many applications and support the effective functioning of application controls. One such area is access security. What is the objective of access security and what are the activities included in it? **(3 Marks)**

**Answer**

- (a) Meaning of Sweat Equity & Disclosure of shares held by Promoters:**

**Meaning Sweat Equity Shares:** According to Section 54 of the Companies Act, 2013, the employees may be compensated in the form of 'Sweat Equity Shares'.

"Sweat Equity Shares" mean equity shares issued by the company to **employees or directors** at a discount or for consideration other than cash for providing know-how or making available right in the nature of intellectual property rights or value additions, by whatever name called.

**Disclosure requirements of such promoter's shareholding:** A company shall disclose Shareholding of Promoters\* as below:

Shares held by promoters at the end of the year				% Change during the year***
S. No.	Promoter Name	No. of shares	% of total shares**	

\* Promoter here means promoter as defined in the Companies Act, 2013.

\*\* Details shall be given separately for each class of shares.

\*\*\* percentage change shall be computed with respect to the number at the beginning of the year or if issued during the year for the first time then with respect to the date of issue.]

**(b) Acceptance of a Change in Engagement:**

The auditor may decide not to send a new audit engagement letter or other written agreement each period. However, **a significant change in nature or size of the entity's business is one of the factors** which may make it appropriate to revise the terms of the audit engagement.

In the given situation, XYZ Limited has diversified its business and few new products have also been introduced by the Company which is indicative of significant change in nature or size of the entity's business. In view of above, CA. P can agree to the request made by the management to change the terms of the audit engagement. Therefore, request of Management to change the terms of audit engagement is appropriate.

**A request from the client for the auditor to change the engagement may result from-**

1. a change in circumstances affecting the need for the service,
2. a misunderstanding as to the nature of an audit or related service originally requested.
3. a restriction on the scope of the engagement, whether imposed by management or caused by circumstances.

**(c) Matters to be considered while designing an Audit Sample:**

As per SA 530, "Audit Sampling",

- (i) When designing an audit sample, the auditor shall consider the purpose of the audit procedures and the characteristics of the population from which the sample will be drawn.
- (ii) When designing an audit sample, the auditor shall determine a sample size sufficient to reduce sampling risk to an acceptably low level.
- (iii) When designing an audit sample, the auditor shall select items for the sample in such a way that each sampling unit in the population has a chance of selection.
- (iv) When designing an audit sample, the auditor shall determine that sample selected must be representative of the population.

- (v) When designing an audit sample, the auditor's consideration includes the *specific purpose* to be achieved and the *combination of audit procedures* that is likely to best achieve that purpose.
- (vi) When designing an audit sample, Consideration of the *nature of the audit evidence* sought and possible deviation or misstatement conditions or other characteristics relating to that audit evidence will assist the auditor in defining what constitutes a deviation or misstatement and what population to use for sampling.
- (vii) In fulfilling the requirement of **SA 500 "Audit Evidence"**, when performing audit sampling, the auditor performs audit procedures to obtain evidence that the population from which the audit sample is drawn is complete.

**(d) Access Security in Automated Environment:**

**Objective of access security:** The objective of Access Security is to ensure that access to programs and data is authenticated and authorized to meet financial reporting objectives.

**Activities:**

- (i) Security Organization & Management
- (ii) Security Policies & Procedures
- (iii) Application Security
- (iv) Data Security
- (v) Operating System Security
- (vi) Network Security – internal network, perimeter network
- (vii) Physical Security – access controls, environment controls
- (viii) System Administration & Privileged Accounts – Sysadmins, DBAs, Super users

**Question 3**

- (a) *The objective of auditing is to design and perform audit procedures in such a way as to enable the auditor to obtain sufficient appropriate audit evidence to be able to draw reasonable conclusions on which to base the auditor's opinion. This can be obtained by performing which procedures? Name the types of audit procedures the auditor can perform to obtain audit evidence?* **(4 Marks)**
- (b) *M/s SS & Associates have been appointed as statutory auditors of Green Limited, a company engaged in the business of manufacturing of hardware products. They are analyzing the monthly trends for other expenses like rent, power and fuel, repairs, etc. and are also verifying attributes of such types of expenses. List down the attributes for verifying such expenses.* **(4 Marks)**
- (c) *While auditing books of accounts of SOLAR Ltd., you observed that an amount due from a debtor for invoice issued on 31.03.2022 has not been recognized in the books of*

*accounts. As an auditor, you want to ensure that all trade receivable balances that are supposed to be recorded have been recognized in the financial statements. How will you achieve the stated objective?* **(3 Marks)**

- (d) *A Ltd. has traded for 50.00 Lacs in "TETRA", a virtual currency, during the F.Y. 2021-2022 and earned a profit of 20.00 Lacs on it. What disclosure requirements are prescribed for such type of transactions done by the company?* **(3 Marks)**

**Answer**

- (a) Audit Procedures to Obtain Audit Evidence:** Audit evidence to draw reasonable conclusions on which to base the auditor's opinion is obtained by performing:

- (I) Risk assessment procedures; and
- (II) Further audit procedures, which comprise:
  - i. Test of controls, when required by the SAs or when the auditor has chosen to do so; and
  - ii. Substantive procedures, including tests of details and substantive analytical procedures.

**Audit procedures to obtain audit evidence can include**

- (a) Inspection
- (b) Observation
- (c) External Confirmation
- (d) Recalculation
- (e) Reperformance
- (f) Analytical Procedures
- (g) Inquiry

- (b) Attributes for verifying other expenses like Power and Fuel, Repair etc.:**

An entity in addition to making purchases and incurring employee benefit expenses, also incurs other expenditures like rent, power and fuel, repairs and maintenance, insurance, travelling, miscellaneous expenses etc., that are essential and incidental to running of business operations.

While the auditor may choose to analyse the monthly trends for expenses like rent, power and fuel, an auditor generally prefers to vouch for other expenses to verify following attributes:

- (a) Whether the expenditure pertained to current period under audit;
- (b) Whether the expenditure qualified as a revenue and not capital expenditure;

- (c) Whether the expenditure had a valid supporting document like travel tickets, insurance policy, third party invoice etc.;
- (d) Whether the expenditure has been classified under the correct expense head;
- (e) Whether the expenditure was authorised as per the delegation of authority matrix;
- (f) Whether the expenditure was in relation to the entity's business and not a personal expenditure.

**(c) Audit of Trade Receivable:**

All Trade receivable balances that were supposed to be recorded have been recognized in the financial statements. (COMPLETENESS): The auditor needs to satisfy himself of the cut-offs. Without a cut-off, sales could be understated or overstated, hence there is a need to perform the following cut off procedure:

- (a) For the invoices issued during the last few days (last 5 days of the reporting year) i.e. cut-off date and which have been included in the debtors; check that the goods should have been dispatched and not lying with the Company;
- (b) Ensure that all goods dispatched prior to the period/ year-end have been invoiced and included in debtors on a test check basis;
- (c) Ensure that no goods dispatched after the year- end have been invoiced and included in debtors for the period under audit.

**(d) Disclosure of Crypto Currency or Virtual Currency:**

Where the Company has traded or invested in Crypto currency or Virtual Currency during the financial year, the following shall be disclosed:

- (a) profit or loss on transactions involving Crypto currency or Virtual Currency
- (b) amount of currency held as at the reporting date,
- (c) deposits or advances from any person for the purpose of trading or investing in Crypto Currency/ virtual currency.

**Question 4**

- (a) *Z Ltd. is a manufacturer of ready-made garments. During the year 2021-22, they have opened two new branches and there is a substantial increase in their sales. The management has appointed CA R to review the internal control system of the company as they feel that there are lapses in the control environment of the company. What is included in the control environment and what will the auditor evaluate in order obtain an understanding of the control environment?* **(4 Marks)**
- (b) *HMB Limited's business has grown from one state of India to various countries of the world. Since the business has increased manifold, the management decided to appoint joint auditors for conducting the statutory audit of the company. They appointed three CA firms for it. For which audit work the joint auditors will be jointly & severally responsible?*

**(4 Marks)**

- (c) *ABC Ltd. has many divisions and branches across the country. They have an internal control system which is well established maintained by the management on a regular basis. Explain the meaning of internal control as per SA-315 and also state the benefits of understanding the internal controls of a company.* **(3 Marks)**
- (d) *As per the Standard on Auditing (SA) 520 "Analytical Procedures", what are the examples of analytical procedures having consideration of relationships?* **(3 Marks)**

**Answer**

**(a) Control Environment:**

The control environment includes:

- i. the governance and management functions and
- ii. the attitudes, awareness, and actions of those charged with governance and management.
- iii. the control environment sets the tone of an organization, influencing the control consciousness of its people.

**The auditor shall obtain an understanding of the control environment.** As part of obtaining this understanding, the auditor shall evaluate whether:

- (a) Management has created and maintained a culture of honesty and ethical behavior; and
- (b) The strengths in the control environment elements collectively provide an appropriate foundation for the other components of internal control.

**(b) Joint Audit of Financial Statements:**

**As per SA 299, "Joint Audit of Financial Statements"**, all the joint auditors shall be jointly and severally responsible for:

- i. the audit work which is not divided among the joint auditors and is carried out by all joint auditors;
- ii. decisions taken by all the joint auditors under audit planning in respect of common audit areas;
- iii. matters which are brought to the notice of the joint auditors by any one of them and there is an agreement among the joint auditors on such matters;
- iv. examining that the financial statements of the entity comply with the requirements of the relevant statutes;
- v. presentation and disclosure of the financial statements as required by the applicable financial reporting framework;



- vi. ensuring that the audit report complies with the requirements of the relevant statutes, applicable Standards on Auditing and other relevant pronouncements issued by ICAI.

**(c) Meaning and benefits of understanding Internal Control:**

**Meaning of Internal Control:** As per SA-315, "Identifying and Assessing the Risk of Material Misstatement Through Understanding the Entity and its Environment", the internal control may be defined as "the process designed, implemented and maintained by those charged with governance, management and other personnel to provide reasonable assurance about the achievement of an entity's objectives with regard to reliability of financial reporting, effectiveness and efficiency of operations, safeguarding of assets, and compliance with applicable laws and regulations. The term "controls" refers to any aspects of one or more of the components of internal control."

**Benefits of Understanding of Internal Control:** An understanding of internal control assists the auditor in:

- i. identifying types of potential misstatements;
- ii. identifying factors that affect the risks of material misstatement, and
- iii. designing the nature, timing, and extent of further audit procedures.

**(d) Examples of Analytical Procedure having consideration of relationship:**

As per the Standard on Auditing (SA) 520 "Analytical Procedures", examples of Analytical Procedures having consideration of relationships are:

- i. Among elements of financial information that would be expected to conform to a predictable pattern based on the entity's experience, such as gross margin percentages.
- ii. Between financial information and relevant non-financial information, such as payroll costs to number of employees.

**Question 5**

- (a) NG Ltd. appointed CA N as the statutory auditor for the F.Y. 2021-2022. Previous year's auditor gave a qualified opinion on the Comparative Financial Statements for the year ended 31.03.2021. What will be the reporting responsibility casted on CA N when he forms an opinion and prepares audit report on the Comparative Financial Statements for the F.Y. 2021-2022? **(4 Marks)**
- (b) M/s RAP & Co., a firm of Chartered Accountants, has three partners, namely Mr. R, Mr. A and Mr. P. Mr. R is also in whole time employment elsewhere and Mr. A & Mr. P do not hold any audits in their personal capacity or as partners of other firms. The Firm, currently, has statutory audit of 40 public companies. They are offered the statutory audit of a public company XYZ Ltd. Whether M/s. RAP & Co. can accept the audit of XYZ Ltd.? **(4 Marks)**
- (c) CAM is the engagement partner of S Ltd. He has instructed his audit team to maintain proper audit documentation. The audit team members are not sure about the purpose for

*which the documentation should be made. Explain the various purposes of audit documentation with reference to SA 230.* **(3 Marks)**

- (d) *You notice a misstatement resulting from fraud or suspected fraud during the audit and conclude that it is not possible to continue the performance of audit. As a Statutory Auditor, how you will deal with this situation?* **(3 Marks)**

**Answer**

- (a) Prior Period Financial Statements Audited by a Predecessor Auditor:** As per SA 710, if the financial statements of the prior period were audited by a predecessor auditor, in addition to expressing an opinion on the current period's financial statements, CA. N, the auditor of NG Limited shall state in an Other Matter paragraph:

- (a) That the financial statements of the prior period were audited by a predecessor auditor;
- (b) The type of opinion expressed by the predecessor auditor and, if the opinion was modified, the reasons therefor; and
- (c) The date of that report, unless the predecessor auditor's report on the prior period's financial statements is revised with the financial statements.

- (b) Eligibility to be appointed as an auditor of a company:** Section 141(3)(g) of Companies Act, 2013 states that a person who is in full time employment elsewhere or a person or a partner of a firm holding appointment as its auditor, if such persons or partner is at the date of such appointment or reappointment holding appointment as auditor of more than twenty companies shall be disqualified from being appointed as auditor of the company.

In the case of a firm of auditors, it has been further provided that 'specified number of companies' shall be construed as the number of companies specified for every partner of the firm who is not in full time employment elsewhere.

The above said ceiling applies per partner of the firm. In the given case, M/s. RAP & Co., a firm of Chartered Accountants, having 3 partners CA. R, CA. A and CA. P, is offered appointment of statutory audit of a public company XYZ Limited. CA. R is in whole time employment elsewhere, therefore, for computation of ceiling limit only CA. A and CA. P (two partners) will be considered. Therefore, entitlement of firm is 40 company audits(20X2) only.

Since, M/s. RAP & Co. is already having statutory audit of 40 public companies, therefore, RAP & Co. cannot accept audit of XYZ Limited.

- (c) Purpose of Audit Documentation:** As per SA 230, "Audit Documentation", the following are the purpose of Audit documentation:

1. Assisting the engagement team to plan and perform the audit.
2. Assisting members of the engagement team to direct and supervise the audit work, and to discharge their review responsibilities.

3. Enabling the engagement team to be accountable for its work.
  4. Retaining a record of matters of continuing significance to future audits.
  5. Enabling the conduct of quality control reviews and inspections in accordance with SQC 1.
  6. Enabling the conduct of external inspections in accordance with applicable legal, regulatory or other requirements.
- (d) **Inability of auditor to continue the engagement:** If, as a result of a misstatement resulting from fraud or suspected fraud, the auditor encounters exceptional circumstances that bring into question the auditor's ability to continue performing the audit, the auditor shall:
- (a) Determine the professional and legal responsibilities applicable in the circumstances, including whether there is a requirement for the auditor to report to the person or persons who made the audit appointment or, in some cases, to regulatory authorities;
  - (b) Consider whether it is appropriate to withdraw from the engagement, where withdrawal is possible under applicable law or regulation; and
  - (c) If the auditor withdraws:
    - i. Discuss with the appropriate level of management and those charged with governance the auditor's withdrawal from the engagement and the reasons for the withdrawal; and
    - ii. Determine whether there is a professional or legal requirement to report to the person or persons who made the audit appointment or, in some cases, to regulatory authorities, the auditor's withdrawal from the engagement and the reasons for the withdrawal.

**Question 6**

- (a) *TS Ltd. has raised funds by issuing fully convertible debentures. These funds were raised for the expansion and diversification of the business. However, the company utilised these funds for repayment of long-term loans and advances. What are the reporting requirements under CARO 2020 in this case?*

OR

*M/s PQ & Co., Chartered Accountants have been appointed as statutory auditor of CBD Multiplex Cinema Ltd. The audit team started the audit and verified the ledger and other books of accounts for the F.Y 2021-2022. However, one of the team members is of the view that the internal control mechanism of the company should also be verified. Can you guide the audit team about the areas that will be covered in verifying the internal control mechanism?*

**(4 Marks)**

- (b) *CARD Ltd. is into the banking business and handles large amount of loans and advances of different kinds. Non-performing assets are on the rise since last two quarters. The*

*management is concerned with correct provisioning for the same. CA R is appointed to check whether correct provisioning of NPA's is being made by the bank or not. What are the aspects that will be verified by CA R for this purpose?* **(4 Marks)**

- (c) *CA Sevak is appointed as an auditor of a Municipal Corporation of a big smart city. He wants to verify various expenditures of the Municipality. Define the term "Municipality" and state what are the heads under which expenditures incurred by the Municipalities and Corporations can be broadly classified?* **(3 Marks)**
- (d) *Ban LLP is formed during the year 2021-22. They are not sure about the type of books of accounts to be maintained. What are the books of accounts that the LLP is required to maintain?* **(3 Marks)**

**Answer**

- (a) Reporting Requirements under CARO 2020 for raising funds:** As per clause (x)(b) of Para 3 of CARO, 2020, the auditor of a company has to report whether the company has made any preferential allotment or private placement of shares or convertible debentures (fully, partially or optionally convertible) during the year and if so, whether the requirements of section 42 and section 62 of the Companies Act, 2013 have been complied with and the funds raised have been used for the purposes for which the funds were raised, if not, provide details in respect of amount involved and nature of non-compliance.

In the present case, TS Ltd. has raised funds by issuing fully convertible debentures for expansion and diversification of the business. However, the company used the funds for repayment of long-term loans and advances instead of utilisation of the same for the purpose for which the funds were raised i.e. expansion and diversification of business.

Here, the auditor should report the fact in his report that the funds were used for the purpose other than the purpose for which the funds were raised, as per clause (x)(b) of Para 3 of CARO, 2020.

**OR**

- (a) Areas to be covered while verifying the Internal Control Mechanism in Multiplex:** Audit Team of M/s PQ & Co. should cover the following areas to verify the internal control mechanism of CBD Multiplex Cinema Ltd.-
- that entrance to the cinema-hall during show is only through printed tickets;
  - that they are serially numbered and bound into books;
  - that the number of tickets issued for each show and class, are different though the numbers of the same class for the show on the same day, each week, run serially;
  - that for advance booking a separate series of tickets is issued; and
  - that the inventory of tickets is kept in the custody of a responsible official.

- (b) **Provisioning of Non-performing Assets:** CA R should verify that the classification of NPAs into sub-standard assets, doubtful assets and loss assets is done depending upon prudential norms as per the RBI Guidelines. Further he should also ensure that provision is being made for the same in accordance with the given table:

<b>Categories of Non-Performing Assets:</b>	<b>Provision required</b>
<b>Substandard Assets:</b> Would be one, which has remained NPA for a period less than or equal to 12 months.	15%
<b>Doubtful Assets:</b> Would be one, which has remained in the substandard category for a period of 12 months.	
<b>Sub-categories:</b> <ul style="list-style-type: none"> <li>• Doubtful up to 1 Year (D1)</li> <li>• Doubtful 1 to 3 Years (D2)</li> <li>• Doubtful more than 3 Years (D3)</li> </ul>	(Secured + Unsecured) 25% + 100% 40% + 100% 100% + 100%
<b>Loss Assets:</b> Would be one, where loss has been identified by the bank or internal or external auditors or the RBI inspection but the amount has not been written off wholly.	100%

**Alternative Answer 1:**

**Aspects to be verified by CA R to check correct provisioning of NPAs:** CA R should verify following aspects while checking whether correct provisioning of NPAs is being made by bank: -

1. It should be verified whether classification of NPAs is in accordance with RBI guidelines. Such guidelines require classification of NPAs into sub-standard assets, doubtful assets and loss assets depending upon different criteria. Each classification requires different percentage of provisions. Therefore, proper classification of NPAs would ensure that provisioning is correct.
2. It should be verified that doubtful assets have been further properly classified in D1, D2 and D3 categories. These three different categories require provision of 25%, 40% and 100% respectively of secured portions of outstanding amount.
3. It should be verified that secured and unsecured portion in doubtful assets have been arrived at properly. Unsecured portion of liability entails provision of 100%. Therefore, it is important to verify that break-up of doubtful assets into secured and unsecured portions is proper.

4. As different kinds of loans and advances are handled by the bank, it should be ensured that loan classification according to its purpose is properly made in the system. NPA norms vary for cash credit accounts, term loans, bills purchased and agricultural loans. Any wrong classification can lead to incorrect provisioning. For example, if an agricultural loan is wrongly classified, it would lead to incorrect provisions.

**Alternative Answer 2:**

Aspects to be verified by CA R to check correct provisioning of NPAs:

1. For audit of Provisions, the auditor should ensure that the compliances for various regulatory requirements for provisioning as contained in the various circulars have been fulfilled.
  2. The auditor should obtain an understanding as to how the bank computes provision on standard assets and non-performing assets. It will primarily include checking the basis of classification of loans and receivables into standard, sub-standard, doubtful, loss and non-performing assets.
  3. The auditor may verify the loan classification on a sample basis.
  4. The auditor should obtain the detailed break up of standard loans, non-performing loans and agree the outstanding balances with the general ledger.
- (c) **Definition of Municipality & Expenditure incurred by it:** **Definition:** A Municipality can be defined as a unit of local self-government in an urban area. By the term 'local self-government' is ordinarily understood the administration of a locality – a village, a town, a city or any other area smaller than a state – by a body representing the local inhabitants, possessing fairly large autonomy, raising at least a part of its revenue through local taxation and spending its income on services which are regarded as local and, therefore, distinct from state and central services.

**Expenditure incurred by the municipalities and corporations can be broadly classified under the following heads:**

- (a) general administration and revenue collection,
- (b) public health,
- (c) public safety,
- (d) education,
- (e) public works, and
- (f) others such as interest payments, etc.

- (d) Books of Accounts Ban LLP is required to maintain: An LLP shall be under obligation to maintain annual accounts reflecting true and fair view of its state of affairs. LLPs are required to maintain books of accounts which shall contain-
1. Particulars of all sums of money received and expended by the LLP and the matters in respect of which the receipt and expenditure takes place,
  2. A record of the assets and liabilities of the LLP,
  3. Statements of costs of goods purchased, inventories, work-in-progress, finished goods and costs of goods sold,
  4. Any other particulars which the partners may decide.